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Unequal lesson for Social Security
By: Rep. Brad Miller and Timothy Smeeding

The coming debate over Social Security may well be a preview of U.S. politics in the 21st century: 99 percent of Americans fighting over reduced benefits and increased taxes, while the richest 1 percent of them remain blissfully unaffected.

There are many explanations for the projected Social Security shortfall in 30 years. Americans are living longer and retiring earlier, for one. There are relatively more retired Americans and fewer Americans in the work force.

But the problem is largely due to increased income inequality.

Social Security is funded by a payroll tax on up to $106,800 a year in wages. Congress set the formula for the cap a generation ago. The aim was to make 90 percent of wages subject to the tax, and index the cap to increases in average wages.

The formula assumed that income distribution would remain roughly the same — that the prosperity from a growing economy would be widely shared. That assumption was spectacularly incorrect.

At the time, the richest 1 percent of Americans took home about 9 percent of all income. But from 1993 to 2007, more than 65 percent of the increase in income went to the richest 1 percent — who now take home almost a quarter of all income. Because wage increases have so disproportionately gone to Americans with wages above the cap, the payroll tax now reaches 83 percent of wages, not 90.

The inequality in all income is even more pronounced. Income from investments is not subject to the Social Security payroll tax. In 2008, two-thirds of dividend income went to Americans making more than $200,000 a year.

A ruthless world economy is only likely to increase wage inequality in the next generation — with more and more income derived from wealth rather than labor. While unemployment has hovered near 10 percent, and wages have remained stagnant, corporate profits have soared to record levels. Based on the last quarter, U.S. businesses are on track to make $1.66 trillion in profits this year.

The Obama deficit reduction commission's plan, Bowles-Simpson, aims to close the projected shortfall. It seeks to raise the cap on wages subject to the payroll tax and by "progressive" cuts in benefits, while laudably creating a minimum benefit for low-wage workers. The result very likely would be that the bottom fifth's benefits would increase modestly and the second fifth would tread water. The top three-fifth's benefits, however, would be cut 10 percent to 20 percent by 2050.

If the increase in income inequality was because the poor were losing ground to the middle class, or even because those in the top fifth were pulling away from those in the bottom 20 percent, Bowles-Simpson's Social Security proposals would be excellent.

There has been little increase, however, in income inequality among the bottom 99 percent since 1993. The yawning gap since is almost entirely the result of the richest 1 percent pulling away from everyone else.

Bowles-Simpson estimates that by 2050, the increase in the cap on wages subject to the payroll tax would result in a maximum increase of a little more than $2,000 a year in payroll taxes. That would not be unbearable for most of the top 20 percent, but it would be noticeable.

The top fifth of seniors do not depend on Social Security benefits as much as those in the bottom 40 percent do. Social Security is 85 percent of the income for the bottom 40 percent of the elderly. For the top fifth, Social Security is 25 percent of income — still a significant portion.

For most of the top fifth, a 20 percent cut in Social Security income — about $5,000 a year — could be a real bite.

But for the richest 1 percent of workers, an additional $2,000 of taxes would be chump change — as would a reduction of benefits by $5,000 for the richest 1 percent of the elderly.

So, Bowles-Simpson "fixes" the problem largely created by increased income inequality by increasing income inequality.

If our options now seem limited, it's because of other political decisions.

The debate a decade ago was not how to reduce the deficit but what to do with the surplus. President Bill Clinton called for using the surplus to "save Social Security first." Instead, Congress passed the Bush tax cuts, massively favoring the richest 1 percent.

There may be a lesson here.

The right dismisses concerns about income inequality as "class warfare." Yet it has played the middle class's economic anxieties for political advantage by stoking resentment of the poor. The right is happy now to have a high-stakes struggle over whether to cut Social Security benefits of the top three-fifths to spare the benefits of the bottom two-fifths — with no one questioning that benefits must be cut.

But that's the wrong fight. The correct fight would put 99 percent of Americans on the same side of the barricades.

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